No. 12734

United States Court of Appeals

For the Ninth Circuit

ADOLPH W. ENGSTROM, Trustee in Bankruptcy for Northwest Chemurgy Cooperative, a corporation, Bankrupt, *Appellant,*

vs.

ARTHUR BENZEL *Appellee.*

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF WASHINGTON, NORTHERN DIVISION

APPELLANT'S REPLY BRIEF

EGGERMAN, ROSLING & WILLIAMS,
DEWITT WILLIAMS,
Attorneys for Appellant.
918 Joseph Vance Building
Seattle 1, Washington.

THE ARGUS PRESS, SEATTLE

No. 12734

United States Court of Appeals

For the Ninth Circuit

ADOLPH W. ENGSTROM, Trustee in Bankruptcy for Northwest Chemurgy Cooperative, a corporation, Bankrupt, *Appellant,*

vs.

ARTHUR BENZEL *Appellee.*

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF WASHINGTON, NORTHERN DIVISION

APPELLANT'S REPLY BRIEF

EGGERMAN, ROSLING & WILLIAMS,
DEWITT WILLIAMS,
Attorneys for Appellant.
918 Joseph Vance Building
Seattle 1, Washington.

THE ARGUS PRESS, SEATTLE

TABLE OF CONTENTS

TABLE OF CASES

TEXTS AND STATUTES

United States Court of Appeals

For the Ninth Circuit

ADOLPH W. ENGSTROM, Trustee in Bankruptcy for Northwest Chemurgy Cooperative, a corporation, Bankrupt, *Appellant,*	No. 12734
vs.	
ARTHUR BENZEL, *Appellee.*	

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF WASHINGTON, NORTHERN DIVISION

APPELLANT'S REPLY BRIEF

Appellee purports to restate the facts and in doing so simply selects a few portions of the Agreed Statement or of the Findings which he deems favorable to his contentions. The pertinent portions of the Agreed Statement and Findings are brief, and appellant submits that a much fairer idea of the facts can be obtained from a reading of the District Court's Findings as *quoted* in appellant's brief, pp. 7, 8 or the Agreed Statement (Tr. 12-15). One result of this suggested approach will demonstrate that the District Court did not adopt "appellee's version of the transaction in question" (Appellee's br., p. 3). As a matter of fact, the Court expressly found against appellee on one of the basic points in appellee's argument, i.e., the contention that title did not pass when the warehouse receipt was delivered on January 3rd, 1947. On this issue the Court found against appellee. Finding II states:

> "On or about January 3rd, 1947, the defendant Arthur Benzel, by endorsing and delivering to Northwest Chemurgy Cooperative a negotiable warehouse receipt covering 1,000 bushels of wheat, *sold and delivered said wheat to said corporation* at the agreed net price, after deducting charges for handling, insurance and storage $72.50, of $6927.50" (Tr. 25). (Emphasis supplied.)

The Agreed Statement shows some discrepancy between the parties solely as to the initial conversation between the agents of the parties. However, in view of the basic principles of construction of the preference statute (set out below) the controlling facts are not what the parties said *but what they actually did and what actually happened.*

Before responding directly to each of appellee's contentions appellant therefore again refers to certain of the salient principles announced by the Supreme Court of the State of Washington in the construction of the preference statute here involved:

SUMMARY OF SALIENT PRINCIPLES OF CONSTRUCTION OF PREFERENCE STATUTE

1. There is a definite cutoff date represented by the beginning of the four months' period,

> "Whatever may have been the law prior to the enactment of the state Preference Act in ~~1914~~ 1941, the ~~enactment of the state Preference Act in 1941, the~~ legislature has now provided with respect to preference payments made in discharge of unsecured credits, a definite cutoff date, represented by the beginning of the four months' period." *Seattle Ass'n of Credit Men v. Hudson Machinery Co.* 135 Wash. Dec. 643 (1950) 214 P.(2d) 681.

2. Absent a claim of priority or statutory lien *or security by agreement of the parties* all inquiry regarding the status of a preferential payment is limited to what takes place within the four months' period,

> "There may be inquiry beyond that date (beginning of the four months' period) with respect to any claim that a preference represents payment of a credit which has priority or lien protection under statute, or which is secured by agreement of the parties. But absent such a claim, all inquiry regarding the status of a preference is limited to what took place within the four months' period. * * * But credits received by the insolvent from the creditor prior to the four months' period, unless enjoying statutory priority or secured in some manner, may not be set off or taken into consideration in any other way, whether or not the insolvent made a profit on the transaction." (Portion in parenthesis supplied). *Seattle Ass'n of Credit Men v. Hudson Machinery Co.* 135 Wash. Dec. 643 (1950) 214 P.(2d) 681.

3. In construing an alleged preferential transaction the court is not concerned with when "payment" is received, but rather with whether or not the property of the corporation was diminished by the alleged preferential transfer,

> "We are, of course, not here concerned with what constitutes payment with respect to the statute of frauds, nor are we primarily concerned with the date when Lone received 'payment' for his corn. Our statutory definition of 'preference' quoted earlier in this opinion, contemplates two kinds of preferences: (1) suffering a judgment,

and (2) a transfer of any of the property of the corporation. No judgment is involved in this case. We are primarily concerned here with whether or not the property of the corporation was diminished by a transfer of corporate property to Lone, and if so was a transfer made more than four months before May 1947, or within that four months. *In deciding the question before us, the word 'transfer' is the key word, not 'payment'.*" (emphasis supplied). *Stern v. Lone,* 32 Wn.(2d) 785, 203 P.(2d) 1074.

4. A preferential transfer occurs when a check is cashed, not when it is delivered,

> "It seems clear to us that no transfer of property was made by the delivery of the check . . . It was when the check was cashed that corporate assets were transferred and a preference made." *Stern v. Lone* 32 Wn.(2d) 785, 203 P.(2d) 1074.

5. The intention of the parties as to whether they intended the extension of credit in the transaction which gives rise to the preferential transfer is immaterial,

> "That the parties did not regard nor intend the transaction as an extension of credit, makes the payment none the less a preference." *Seattle Ass'n of Credit Men v. Daniels,* 15 Wn.(2d) 393, 130 P.(2d) 892.

Having the foregoing principles, and the others set forth in appellant's Opening Brief, in mind, we turn now to consideration of the contentions set forth in appellee's Answer Brief.

APPELLEE'S INTRODUCTORY STATEMENT

1. The transaction was not a cash transaction. On the facts Whitemore denied that it was to be a cash transaction (Tr. 13). The facts sustain Whitemore. Williston defines a cash transaction as a sale wherein the seller "declines to transfer either title or right to possession until he is paid" 2 Williston on Sales (Rev. Ed.) 324, §341. The Court found that the wheat was sold and delivered on January 3rd, 1947—appellee was not paid until February 3rd, 1947. Appellee made no effort to suspend title until he was paid. If appellee had intended that title not vest until after he was paid, he would have placed the negotiable warehouse receipt in escrow or sent it to the bank for delivery upon payment to his account, or one of several other alternative methods of obtaining actual payment prior to or at the time of delivery of the negotiable warehouse receipt which vested title. The letter transmitting the warehouse receipt (Ex. A, Tr. 16-17) did so with no reservations, and by the postscript recognized that a check would not be mailed until after the warehouse receipt was received by Chemurgy.

The seller did not accept a check delivered or dated the same day as the delivery of the wheat. *The check he received and accepted was issued, dated and received ten days after he had unconditionally delivered the wheat. These basic facts in themselves completely distinguish the facts of this case from all of the cases relied upon by appellee,* since in appellee's cases delivery of title was usually induced by the delivery of a check dated and delivered on the day the property involved was delivered.

Furthermore, appellee held the check for four days before he even deposited it for collection (Tr. 14)—a further indication that payment was not a condition precedent to the passing of title. Chemurgy was in the business of manufacturing wheat into glucose and it cannot be inferred under the facts of this case that it was restrained from using the wheat purchased from Benzel until such time as appellee condescended to pass title to the wheat by the cashing of Chemurgy's check.

2. *The principle that payment by check suspends the passing of title and that upon non-payment of the check the property can be reclaimed (where the interests of creditors are involved) is not the law in Washington—Goodwin v. Bear,* 122 Wash. 49, 209 Pac. 1080.

Even where the principle is applied it is invoked only in true *cash sales*—and this transaction was not a *cash sale.*

As shown later in this brief under the reply to appellee's contention III, even if appellee had a right at one time to reclaim the wheat (which is not conceded) he waived such remedy prior to the four months' period and chose to look to Chemurgy as his debtor.

The sole ultimate question is whether the property of an insolvent corporation was diminished on February 3rd, 1947, *when money was paid out of its bank account to appellee.* Under the law applicable to the facts of this case on February 3rd, 1947, appellee had no more than a general claim against Chemurgy in the amount of the net price of the wheat and when this claim was paid the property of the insolvent was of course diminished by the amount of said payment.

I.

Appellee contends (Appellee's br., p. 7):

In the absence of an agreement to the contrary it is presumed that a sale of personal property is a cash sale.

Appellant has shown at pages 21 to 32 of the Opening Brief that the transaction here involved was not a "cash sale."

There is no room for *presumptions* in this case as to the vesting of title. The *statutes* under which title vested in Chemurgy are quoted on pages 22 and 23 of appellant's opening brief.

These statutes are, of course, by their terms applicable to endorsements and deliveries of warehouse receipts between the immediate parties. At pages 19 and 20 of his brief appellee cites certain sections of the Washington statutes with respect to bills and notes (R.R.S. 3449, 3419 and 3407) which have no relevance to the statutes quoted on page 22 of appellant's brief. Lest there be any suggestion that the warehouse receipt statutes are not given full effect between the immediate parties we refer to the case of *Klock Produce Co. v. Diamond Ice & Storage Co.,* 90 Wash. 67, 155 Pac. 414, in which it was contended that Rem. Rev. Stat. 3616 requiring endorsement upon the negotiable receipt of charges for storage subsequent to the date of the receipt was not applicable to the original parties to the receipt. The Supreme Court in refusing to follow this argument stated in part:

> "Finally it is argued that, granting that Section 30 (Rem. Rev. Stat. 3616) forbids belated surcharging of a negotiable receipt, the statute really was

looking to the protection of third parties, and that in this suit between original parties the court should give the warehouseman this surcharge. Such doctrine, often tempting to courts, generally lead, though, to embarrassment. If we should let the rule vary in this way we should justify endless contentions as to whether a receipt alleged to be transferred was transferred in good faith, whether the assignment was in legal form, whether the warehouseman had actual notice of it when it was not in legal form, whether the transfer was for value, together with many other contentions that would frequently expose true transferees to loss on technical grounds or put them to laborious proofs which, if we let this statute speak for itself, the paper in his hands would spare him."

"The statute itself is simple. It will cause no hardship on the warehouseman or anybody if let alone * * * The policy of the law was to make negotiable receipts useful in the highest degree."

Following these statutes, the cases all hold that title is transferred immediately upon endorsement and delivery of a negotiable warehouse receipt. Representative quotations are as follows:

"The indorsement of the warehouse certificates to the bank transferred the legal title to the wheat and products which they represented. The warehouse certificates so read, the statutes of Iowa so provide, and such is the general law in the absence of statute. Section 3138a41, 1913 Supp. to Code of Iowa; *Gibson v. Stevens,* 8 How. 383, 12 L.ed. 1123; *Dale v. Pattison,* 234 U.S. 399, 34 Sup. Ct. 785, 58 L.ed. 1370, 52 L.R.A. (N.S.) 754." *Central State Bank v. McFarlin,* 257 Fed. 535, 537.

> "When the appellant became the holder of the receipt for the cotton it acquired such title to the cotton as the person negotiating the receipts to it had the ability to convey and it became the appellee's duty to hold possession of the cotton for him 'as fully as if' it 'had contracted directly with him'. §41, C. 218, Laws of 1920 (Hemingway's Supplement of 1921, §7957 ol)" *Love v. People's Compress Co.* (Miss.), 102 So. 275.

Title was therefore, by virtue of the endorsement and delivery of the warehouse receipt and the applicable statutes of the State of Washington immediately vested in Chemurgy. An examination of all of the cases cited by defendant will show that in none of them was a negotiable document of title involved as to which there was a controlling statute mandatorily transferring title upon endorsement and delivery of the document of title. Since this last statement is applicable to every case cited by defendant and effectually distinguishes every one of defendant's cases from the one here before the court, we will not discuss separately the cases cited by defendant which are therefore not in point and not controlling here. The distinction, for instance, is emphasized in the case of *Quality Shingle Co. v. Old Oregon L. & S. Co.,* 110 Wash. 60 187 Pac. 705, in which the court makes much of the fact that the transfer to the defendant was by *non-negotiable* bill of lading which by statute was specifically subject to existing equities. There is no such limitation on the statutes above quoted applicable to the endorsement and delivery here involved and the *Klock* case above referred to amply demonstrates that the statutes are to be strictly applied in accordance with their terms.

It is obvious that whenever a suspension of title in a sale occurs when the parties have not spoken of the point, it is done as an inference of law where there is no statute governing the situation. However, in this case we have express statutes under which title vested immediately upon the endorsement and delivery of the warehouse receipt. It is therefore pointless to consider cases as authoritative here which do not involve and are not controlled by statute. Since title vested on January 3rd, 1947, and payment was not made until February 3rd, 1947 (or within the four months' period), it is obvious that during said period Chemurgy owed defendant for the wheat and since money was owed to him he was, of course, a creditor.

In support of this contention appellee also cites Rem. Rev. Stat. §5836-42 (Appellee's br., p. 8). But this statute is expressly on the premise:

> "Unless otherwise agreed, delivery of the goods and payment of the price are concurrent conditions;"

It has already been pointed out that delivery of the goods and payment were not to be concurrent in this case. The Court found the property was sold and delivered on January 3rd, 1947. The check was not to be delivered until after title had been conveyed to Chemurgy (See postscript to Ex. A, Tr. 16-17). The discussion between the agents of the parties is immaterial—reference to a cash sale does not make the agreed acts a cash sale.

The case of *Gustafson v. Equitable Loan Association,* 186 Minn. 236, 243 N.W.106, cited by appellee (p. 9)

is not relevant. This was a replevin case arising only on demurrer. The court held that under the pleadings title to the property involved did not pass. Under the Washington statutes quoted on page 22 of the Opening Brief title did pass in the present case. In the *Gustafson* case the court clearly indicated that its result would have been different if title had passed. The court stated:

> "Defendant argues that plaintiff waived the cash payment by voluntarily delivering the diamond and hence title passed to Madden. *In many cases such a question may be one of fact but upon the record before us the contention is untenable;* the pleading is definite; that is all we have." (Emphasis supplied.)

In the present case title passed on January 3rd, 1947, not only as a matter of fact, but also as a matter of statutory law.

The point that this was not a cash sale is discussed on pages 21 to 33 of the Opening Brief.

II.

Appellee contends (appellant's br. p. 10):

> *Upon a cash sale payment by check is conditional only and between the immediate parties title in the buyer does not become absolute until the check is paid.*

In support of this proposition appellee cites *Quality Shingle Co. v. Old Oregon Lumber & Shingle Co.,* 110 Wash. 60, 187 Pac. 705; *Standard Investment Co. v. Town of Snowhill* (N.C.) 78 F.(2d) 33 and *J. W. Young v. Harris Cortner Co.,* 152 Tenn. 15, 268 S.W. 125.

The *Quality Shingle Co.* case is not in point, but if deemed to be, it has been in effect over-ruled by a later Washington case hereinafter referred to. In the *Quality Shingle* case the court relies upon the *express representation* to the seller that the check would be paid upon presentation. On this basis the court stated:

> "It seems to us to follow in the light of elementary rules of law that as between respondent and Shepard-Traill Co. the title to the shingles did not pass from respondent to Shepard-Traill Co. upon it receiving the bill of lading for the shingles and giving its check to respondent therefor."

The case is irrelevant here because there was no false representation in the present case and because the District Court by its findings found that the wheat had been "sold and delivered to Chemurgy" (Tr. 21).

The later case of *Goodwin v. Bear,* 122 Wash. 49, 209 Pac. 1080 demonstrates that it is not the rule in Washington (and therefore not the rule of this case) that title is suspended pending the payment of a purchase price check. In that case the appellant sold 12 cows to one Tarry. By agreement the cows remained on appellant's farm until Tarry wanted them. Six days later Tarry gave appellant his check for the balance of the purchase price and two days later Tarry took the cows from appellant. Appellant kept the check four days and then deposited it for collection. Before the check was paid by Tarry's bank the respondent, Central Bank & Trust Company, seized the cattle under an execution upon a judgment against Tarry. Tarry then stopped payment on the check and through his agent advised appellant that he should make claim for the cattle. Ap-

pellant brought this action in replevin. The trial court held that title passed at the time of the original purchase on August 17, 1921, and rendered judgment against appellant. Appellant contended that a check cannot be considered as payment untill it is made good and cited cases holding that a worthless check is not in fact payment and that goods so obtained can be reclaimed. The court, in affirming the trial court and repudiating the appellant's contention stated:

> "There is no evidence in this case indicating that the check was not drawn against sufficient funds and the evidence further shows that the parties intended a completed sale on August 17. *If appellant intended to keep the possession of the cattle as security for his final payment he lost his right to a lien when he permitted the cattle to be taken from the premises and thus surrendered his possession.* His delay of four days in presenting his check prevented it being paid in the ordinary course of business and if he were permitted to prevail in this action he would carry into effect the apparent effort of Tarry to defraud his creditor, the respondent bank."

Applying the foregoing case to the present case it shows the irrelevancy of appellee's worthless check cases, demonstrates further the title to the wheat here involved passes on January 3, 1947, when it was delivered and also demonstrates that appellee's delay in presenting his check cannot be used to defeat the obvious application of the Washington Preference Statute in favor of Chemurgy's creditors. It will be remembered in the present case (Tr. 14) that Benzel also waited four days to deposit his check. There is no evidence that the funds

of Chemurgy were insufficient when the check was delivered or during the days in which Benzel delayed in depositing it. The case of *In re A. O. Brown & Co.,* 189 Fed. 442 (cited by appellee, p. 13) demonstrates that the non-payment of a check does not indicate fraud where a period of time (as in the present case) must necessarily elapse between the mailing of a check and its presentation for payment. The court stated:

> "It is doubtless the custom to deposit checks and so to take 24 hours to cash them, and, if that were a part of the engagement so that the check could not be presented for payment except at the end of 24 hours, then the check would properly be held to be a time draft; and, though the time would be short, it would be also quite proper to hold that to give the check was no more than a representation that at the end of 24 hours the drawee would be in funds. *Were that the fact, it would be impossible to show fraud or a misrepresentation of fact without showing that the drawer did not intend to put the drawee in funds when he uttered the check.*" (Emphasis supplied.)

The court in the *Brown* case also expressed disapproval of those cases which hold that delivery by a seller upon a cash sale (assuming solely for the purpose of argument that a cash sale was made in the instant case) is not of itself a waiver of the condition of payment. The court stated:

> "In the other cases the rule seems to be confused with the rule which exists in many jurisdictions that delivery by a seller upon cash sale is not of itself a waiver of the condition of payment. *I believe that this rule is quite wrong in principle*

(Williston on Sales, §346); nor is there any authority binding upon me. *At least such a delivery must be held to be presumptive evidence of waiver and this appears to be the rule in New York. Osborn v. Gantz,* 60 N.Y. 540." (Emphasis supplied.)

Williston also is very critical of the cases which hold that vesting of title is conditional until a check representing the purchase price is paid. Williston states:

"It is submitted that such decisions are unsound. The reasoning upon which they rest is that a worthless check is no payment of the price, and the condition has not happened upon which the property was to pass. *But the real question is, did the seller assent to transfer the ownership in the goods; and it can hardly be doubted that he did.* If it were true as is often stated, that the fact that the check is given merely in conditional payment proves that no title passes until the condition is satisfied, the same consequence would follow if a time draft were given instead of a check. *Such a result would obviously be absurd. It would also follow that where a check was given and there were funds to meet it, no title would pass until the check was paid,* for a good check as well as a bad check is generally held only conditional payment. *There is confusion of thought in supposing that the condition in conditional payment by means of negotiable paper has any reference to the ownership of property given in exchange for the paper.* The condition relates to the creditor's right to revert to the money claim for which the negotiable paper was given. If a seller should say, 'you must not deal with these goods, though I have put them in your hands, until I collect the check,' *that* would show an intent not to transfer the property to the buyer. *But when the*

goods are put into the buyer's hands without more, it can hardly be doubted that the seller means to allow him to deal with them as his own; to resell them immediately if he feels inclined. If no title passed until the check was paid the buyer would be a tort feasor if he used the goods until the check was paid, even though there were ample funds in the bank to make the payment." * * *

"A delivery to the buyer with authority to use the goods immediately should be conclusive evidence of transfer of the property in the absence of clear evidence, showing an intention to reserve the title." 2 Williston on Sales, Revised Ed. 346 (a) and 346 (b).

As shown above in the *Bear* case the Washington court, in line with Williston's comments, holds that after possession is given title is not suspended pending the payment of a purchase money check.

The case of *Standard Investment Co. v. Town of Snowhill* (N.C.) 78 F.(2d) 33, (cited by appellee, p. 11) holds that title does pass subject only to a right of recision if the check is not paid. The court stated:

"Until the check is itself paid, the title as between the parties, passes only conditionally; and upon dishonor of the check, the seller may rescind the transaction and reclaim that with which he has parted."

The case of *Young v. Harris Cortner Company,* 152 Tenn. 15, 268 S.W. 125, (cited by appellee, p. 12) is also not in point on the facts because in that case a check was delivered immediately at the time of delivery of the cotton there involved and the court held that:

"Upon principle we are unable to distinguish

> the instant cause from that of a sale made over a counter where the seller was induced to accept a check as cash."

In the instant case the wheat was delivered under circumstances clearly demonstrating that a check was not to be given until sometime later and after computations had been made to arrive at the net price. The *Young* case also relied upon the doctrine that in such cash sales title does not pass, which doctrine is criticized by Williston as set forth above, and not followed in Washington as shown by the *Bear* case reviewed above. Appellee at page 13 refers to the fact that the sales in the *Young* case were represented by negotiable warehouse receipts but appellee fails to point out that the court held the receipts *not negotiable* because of falsehoods appearing thereon. The court stated:

> "They are not in a position therefore to rely upon said receipt because it speaks a falsehood of which they had knowledge" (The falsehood was that wheat had not been deposited when the receipts were issued.)

The statute quoted by appellant (Appellant's Brief p. 22) applies to *negotiable* warehouse receipts.

III.

Appellee contends (appellee's br. p. 13):

"Where a seller accepts payment of goods by a check dishonored on presentation, the seller may either recover the proceeds of the sale or retake the property from a trustee in bankruptcy of the buyer."

This contention is in no event applicable in this case because of the express holding of the Supreme Court of

the State of Washington in construing the preference statute (which construction is, of course, binding in this case) that every payment out of the funds of an insolvent corporation during the four months period is deemed a preference *unless paid on a claim having priority, or a claim having lien protection under a statute, or a claim which is secured by agreement of the parties*:

> "There may be inquiry beyond that date (beginning of the four months period) with respect to any claim that a preference represents payment of a credit which has priority or lien protection under statute or which is secured by agreement of the parties. But absent such a claim all inquiry regarding the status of a preference is limited to what took place within the four months period." *Seattle Association of Credit Men v. Hudson Machinery Co.,* 135 Wash. Dec. 643, (1950) 214 P.(2d) 681.

The alleged right of the appellee could not, of course, under any circumstances qualify under the foregoing quotation as a prior claim or a statutory lien claim or a claim "*secured by agreement.*" Furthermore, the doctrine of the cases listed on page 13 of appellee's brief is in any event only applicable in *cash sales* where the passing of title is conditioned upon the payment of the purchase price.

There are good reasons for the Washington court's construction as aforesaid of the preference statute.

The law abhors secret liens or rights. If this court were to find that this was *a conditional sale,* and give effect to such agreement on any theory, the court would be upholding a secret lien or right and would, at the

same time, destroy to a large extent the effectiveness of the preference act. If a party can "sell and deliver" property (Tr. 25) and *by inference* still retain secret rights therein which can be asserted as against representatives of all creditors, then he can do so by oral agreement, and as a result any creditor could make a deal with his insolvent debtor which would result in his getting a greater percentage of his debt than other creditors of the insolvent. To avoid the impact of the preference statute, the debtor and creditor, if appellee's position is sound, need only testify that they made a secret oral agreement which had the effect of reserving title and giving the creditor preferred status. The impossibility of meeting such evidence is obvious. Appellee here attempts to *infer* a secret right, which should not be given effect, even if orally agreed upon.

The policy of the Federal Bankruptcy Act, to which the Washington court has made frequent reference (*Seattle Ass'n of Credit Men v. Hudson Machinery Co.* 135 Wash. Dec. 643, 214 P.(2d) 681) is to require creditors to use orthodox methods of establishing and retaining legal rights and liens (Chap. 70, Public Law, 461, U. S. Code Cong. Service, 1950, page 185). The purpose of §60-A,(6), the section promulgating the aforesaid policy is:

> "To make it certain that the amendment (to the Federal Bankruptcy Act giving greater security to power of sales security transactions) will not validate, in the hands of a secured creditor, equitable liens where available means of proving legal liens have not been employed by him." U.S. Code Cong. Service 1950, House Report No. 1293, P. 263, 267. (Parenthetical portion supplied)

The State of Washington requires the recording of conditional sales, Rem. Rev. Stat. § 3790.

We have already shown at pages 21 to 32 of the opening brief that the transaction here involved was not a "cash sale."

Assuming, however, simply for the purposes of the argument, that title to the wheat was originally only conditional and that originally appellee had a right to reclaim the wheat, still under well settled and leading authority title vested unconditionally without right of any reclamation because appellee failed to act promptly upon breach of the conditions upon which he relies.

Title vests even when a sale is on condition unless the seller acts promptly upon breach of condition and further vests whenever there is a failure of initial payment and possession is allowed to be retained upon a new promise to pay.

A leading case on this point is *Frech v. Lewis,* 218 Pa. 141, 67 Atl. 45 involving the sale of two carriages to be paid for on delivery. Payment was not made on delivery and seller did not promptly move to reclaim the property. In an action of replevin to regain possession the court found for the defendant on the ground that title had unconditionally passed without right of reclamation. The court stated:

> "Possession, however, having passed, and the buyer, by the act of the seller, having been invested with the indicia of ownership, the policy of our law requires that this situation—the possession in one and the right of property in another—shall continue no longer than is necessary to enable the seller

to recover the goods with which he has parted. The law gives the seller the right, in such case, to reclaim his goods; but he must do so promptly; otherwise he will be held to have waived his right, and can only thereafter look to the buyer for the price. The question the present case suggests is: When does this inference of waiver arise? Our authorities admit of but one answer: Except when delayed by trick or artifice, *the assertion of the right to reclaim the property must follow immediately upon the buyer's default.* This does not mean that the seller must eo instanti begin legal proceedings to recover the goods; but it does mean that the seller, when he discovers that his delivery is not followed by payment, as he had the right to expect, *is at once put to his election whether he will waive the condition as to payment and allow the delivery to become absolute, or retake property;* and that he is to allow no unnecessary delay in making his choice. *The object of the law is not to multiply his remedies because of his disappointment. He may not continue to hold his right to the goods, and at the same time hold the buyer as his creditor. One or the other he must relinquish, and do it promptly, or the law will forfeit his right to elect. Continued acquiescence in the buyer's possession of the goods will be taken as a choice on his part to regard the delivery as absolute, notwithstanding the buyer's default.* The policy of the law, in requiring promptitude in the assertion of continued ownership of the goods, could easily be vindicated were it necessary. It answers every purpose here to show that the law requires it. In *Leedom v. Philips,* 1 Yeates, 527, it is said: 'When the parties specially agree, it is obvious that the vendor may, by his contract, renounce the benefit of the conditions stipulated, and trust to the good

faith of the vendee for a future performance on his part. If one sells goods for cash, and the vendee takes them away without payment of the money, the vendor should immediately reclaim them by pursuing the party; and he may justify the retaking of them by force.' This was quoted approvingly in *Bowen v. Burk,* 13 Pa. 146; and it was there added that, 'where he (the seller) lies by, and makes no complaint in a reasonable time, he consents to the absolute transfer of the property, and the contract is consequently complete against all the world.' In *Backentoss v. Speicher,* 31 Pa. 324, reference is made to the case last above cited. What we have quoted from it was there approved, and the necessity for an immediate reclamation of the goods was emphasized. It is there said: 'This is the principle that is decisive against the present plaintiff. A sale of goods for cash is, strictly speaking, a sale on condition. The contract is do ut des. The condition is more imperative than such as was in this case, but for that reason, less easily waived; and yet if the vendor acquiesce in a possession obtained in disregard of the condition, he waives it, *and, though he may recover the price by action,* he cannot recover the goods in specie . . . When the plaintiff found his condition disregarded, he should have promptly reclaimed the goods.' *Mackaness v. Long,* 85 Pa. 158, is another recognition of the same doctrine that, unless reclamation of the property be made immediately, the title passes to the buyer. These cases and others that might be cited, following the lead of *Leedom v. Philips, supra, all hold that the duty is upon the seller, if he would retain his right to the property, to proceed promptly; and we know of no case in which a contrary doctrine is asserted.* In some cases the expression,

'within a reasonable time,' is used where the right to reclaim is referred to; but this expression suggests no departure from the rule as declared in *Leedom v. Philips, supra.* By 'reasonable time' is to be understood such promptitude as the situation of the parties and the circumstances of the case will allow. *It never means an indulgence in unnecessary delay, or in a delay occasioned by the vain hope and fruitless effort to obtain the money from the defaulting buyer. When the delay is to be accounted for by the latter consideration, it is accepted as an acquiescence in the delivery and the acceptance of the buyer as a debtor.*'' * * *

''The title to a chattel passes as fully after a conditional delivery, where possession is allowed to be retained in consideration of a new promise to pay, as where delivery is preceded by actual payment. The plaintiff was not tricked into delivering the carriages to the defendant, nor was his delay in asserting claim to the property in consequence of any fraud practised. He reposed confidence in the promise of the defendant, and was disappointed. His disappointment does not restore to him the right of property with which he parted. The court below submitted it to the jury to determine whether plaintiff, by his conduct, had waived his right to retake the carriages. The jury found he had not, and gave the plaintiff a verdict for the property. On appeal to the superior court, the judgment of the lower court was affirmed. The ground on which the affirmance rested is thus stated by the learned judge who delivered the opinion: 'It cannot be said, as matter of law, that the plaintiff's conduct amounted to a waiver of his right. In view of the repeated promises of the defendant, the plaintiff might well have been misled and induced to post-

pone proceedings for the recovery of his property. His delay is evidence . . . of a waiver, but it is not conclusive in view of the conduct of the defendant.' (32 Pa. Super. Ct. 282) In this we cannot concur. The reasons for our dissent fully appear in what we have already said. Reliance upon a subsequent promise to pay, that leads the seller to refrain from asserting his right to retake the property, is in itself a waiver of the right, and makes absolute a delivery which in the first instance was conditional. *The right of plaintiff to recover back his property after he had delivered it resulted from the buyer's failure to keep his first promise. His failure to keep subsequent promises to pay could neither prolong nor revive that right.* What defendant did or did not do is a matter that has no place in the inquiry; *what the plaintiff did or failed to do is the determining consideration.* (Emphasis supplied.)

It will be noted from the foregoing case that when the condition of the sale (here assumed to be for the purposes of argument, the prompt delivery of a check) is not met, the seller must move immediately to reclaim the property, otherwise the title vests. Title also vests for another reason, that is where the seller relies on a new promise to pay and certainly in this case the request to redeposit the check amounted to a new promise to pay by that procedure. This case is then in this respect like the *Frech* case just quoted, in that the seller instead of reclaiming his merchandise reposed confidence in the promise of the purchaser. The seller in this case is no different from the sellers of all of the merchandise who have been required in this bankruptcy proceeding to return the purchase price which they received under

the preference statute. They too were disappointed in that they were not paid and payment was deferred into the vital four months' period. The salient fact remains that possession vested in Chemurgy on January 3rd or 4th and it was not until a month later that Benzel was paid. During this interval he took no steps whatsoever to reclaim the possession, took no action because the check was not delivered immediately or because the check was not initially paid and under the well-settled principles enunciated in the foregoing *Frech* case must in any event be deemed to have vested title in Chemurgy on two grounds: (1) By failure to take any action when the check was not delivered as agreed and (2) When the check was not initially paid he did not attempt to reclaim the wheat but proceeded upon Chemurgy's promise that he would be paid and redeposited the check. A further circumstance of course is that Benzel held the check when he first received it for a period of four days before depositing it.

We here state (still assuming only for the purpose of the argument that title had not vested by virtue of the facts and the applicable statutes) that Benzel was put to an election earlier than the dishonoring of the check. The failure for a period of ten days to even receive the check was the breach of even an earlier, (in point of time of execution) agreement so far as performance was concerned and Benzel's taking and depositing the check, after holding it for four days, certainly indicates that he no longer relied upon any conditions but was satisfied with his confidence that he would ultimately be paid.

In *Guarantee Title & Trust Co. v. First National Bank* (3 C. C. A.) 185 Fed. 373 at p. 380, the court approves the doctrine of the *Frech* case and after quoting from the case states:

> "We do not think this view of the law is peculiar to Pennsylvania. It is reasonable, and accords with the practical conduct of human affairs. Delivery to the buyer may conveniently be made without insisting upon the concurrent payment of the price, if this right of reclamation to be promptly and reasonably exercised, is recognized in the seller. Such possession by the buyer, however, is very different in fact and in theory from the vendee's possession which accompanies a conditional sale. It may well be that the insertion by the Car Company, of the reservation of title until payment, in the invoice, was an appeal to and assertion of this right of reclamation, for its protection, after it had surrendered the goods to the possession of the vendee without having received the payment, as stipulated in the contract of sale. But this right of reclamation, as stated in the case just referred to, must be promptly asserted, or it will be considered as waived, and the seller is remitted to his rights against the buyer as his debtor. *Mackaness v. Long.* 85 Pa. 158, is another recognition of the same doctrine, that, unless reclamation of the property be made immediately, the title passes to the buyer. There can be no question, therefore, in the case at bar, that this right of reclamation existing in the Car Company when it allowed the goods sold to be delivered, without the payment it had a right to demand, to the vendee, has been lost by want of assertion during the long period that elapsed between the delivery of the goods and the bankruptcy of the vendee."

In *Cincinnati Railway Supply Co. v. Hartlieb et al.* (6 C. C. A.) 214 Fed. 177, the Circuit Court by per curiam decision, affirmed the District Court, which court quoted and followed the *Frech* case and stated in part:

> "But assuming that they could be traced, or even assuming that the actual goods were still in the hands of the trustee, it has been established by a long line of authorities that such a condition precedent may be waived by circumstances showing an intention to deliver notwithstanding the condition which could have been insisted on, *and to look to the vendee as a debtor only.*" * * *
>
> "The point is made that there was no consideration for the abandonment by the vendor of its initial right to repossess itself of its goods upon vendee's failure to comply with the condition of payment. It is significant that this question was not discussed in any of the numerous cases holding that the circumstances determine whether the vendor's initial right of retaking the goods has been abandoned by him. But the changed relation of the parties are not such as depend upon a new consideration, for the transaction is either one of conditional sale, if the vendor insists upon the condition, or an unconditional sale, depending upon his right to make it one or the other, at his election. *If he elects to waive his right of immediate payment, then the relation of debtor and creditor arises, a relation created by the voluntary act of the vendor and growing out of the voluntary abandonment of the right to treat the sale as conditional.* It is a matter of grace to the vendee involving the voluntary considerations and impulses which impel the making of a gift. *Besides, the vendor may prefer to treat*

the goods as sold and make his profit out of the sale rather than to take back the goods. Indeed, this is exactly what happened in this case as all the facts show. That advantage to the vendor would be a consideration for his conduct in electing to treat the property as sold unconditionally. There is no room to doubt the correctness of the referee's conclusion under the circumstances of this case, and the petition for review will be dismissed at the intervener's costs." 214 Fed. 177, at p. 179. (Emphasis supplied.)

As pointed out in the foregoing quotation, upon the waiver of the condition the Seller becomes a "Creditor" and the Purchaser a "Debtor." The word "Creditor" as used in the Washington preference statute can certainly not be restricted to the narrow meaning attempted to be attributed to it by the defendant in his memorandum. Defendant would say that the only persons who may be considered "Creditors" under the preference statute are those who have specifically agreed that a debtor may have a period of time to pay. No such construction has ever been placed upon the preference doctrine in this state either before or after the enactment of the preference statutes. The word "Creditor" has a very broad meaning and certainly includes one to whom money is owned for any reason.

(See cases in appellant's opening brief, p. 14.)

Obviously in applying the term creditor as used in the preference statute there is absolutely no reason to distinguish between those who have obligations arising by reason of express contractural extensions of time to

pay and those who are simply entitled to be paid an amount for any reason. The gist of the preference statute is not the history of the obligation which is paid but rather that the assets of the corporation upon insolvency become a trust fund which cannot be paid to anyone to whom an obligation is owed.

A sample of the application of the preference doctrine to an instance where there is no extension of credit but simply an obligation implied by law is *Hill v. Brandes,* 1 Wn.(2d) 196, 95 P.(2d) 382, in which the indebtedness arose not out of the extension of credit but because the insolvent corporation had received money to which the defendant was entitled and later in recognition of this obligation made payments which were held to be preferential and recoverable by the receiver. The nature of the case is indicated by the following quotation from the syllabus:

> "Payments made by an insolvent corporation to a finance company constitute unlawful preferences, where the corporation sold automobiles under conditional sales contracts and sold and assigned the contracts to a finance company, and the customers later returned the automobiles to the corporation in trade for other cars and transferred to it their rights under the contracts, and the corporation resold the automobiles for the amounts of the unpaid balances on the contracts and placed the proceeds of such resales in its general bank account, where they became commingled with other funds, and, within four months prior to the appointment of a receiver for the corporation, made payments by checks on its general bank account to the finance company for the balances due on such contracts;

the goods as sold and make his profit out of the sale rather than to take back the goods. Indeed, this is exactly what happened in this case as all the facts show. That advantage to the vendor would be a consideration for his conduct in electing to treat the property as sold unconditionally. There is no room to doubt the correctness of the referee's conclusion under the circumstances of this case, and the petition for review will be dismissed at the intervener's costs." 214 Fed. 177, at p. 179. (Emphasis supplied.)

As pointed out in the foregoing quotation, upon the waiver of the condition the Seller becomes a "Creditor" and the Purchaser a "Debtor." The word "Creditor" as used in the Washington preference statute can certainly not be restricted to the narrow meaning attempted to be attributed to it by the defendant in his memorandum. Defendant would say that the only persons who may be considered "Creditors" under the preference statute are those who have specifically agreed that a debtor may have a period of time to pay. No such construction has ever been placed upon the preference doctrine in this state either before or after the enactment of the preference statutes. The word "Creditor" has a very broad meaning and certainly includes one to whom money is owned for any reason.

(See cases in appellant's opening brief, p. 14.)

Obviously in applying the term creditor as used in the preference statute there is absolutely no reason to distinguish between those who have obligations arising by reason of express contractural extensions of time to

pay and those who are simply entitled to be paid an amount for any reason. The gist of the preference statute is not the history of the obligation which is paid but rather that the assets of the corporation upon insolvency become a trust fund which cannot be paid to anyone to whom an obligation is owed.

A sample of the application of the preference doctrine to an instance where there is no extension of credit but simply an obligation implied by law is *Hill v. Brandes,* 1 Wn.(2d) 196, 95 P.(2d) 382, in which the indebtedness arose not out of the extension of credit but because the insolvent corporation had received money to which the defendant was entitled and later in recognition of this obligation made payments which were held to be preferential and recoverable by the receiver. The nature of the case is indicated by the following quotation from the syllabus:

> "Payments made by an insolvent corporation to a finance company constitute unlawful preferences, where the corporation sold automobiles under conditional sales contracts and sold and assigned the contracts to a finance company, and the customers later returned the automobiles to the corporation in trade for other cars and transferred to it their rights under the contracts, and the corporation resold the automobiles for the amounts of the unpaid balances on the contracts and placed the proceeds of such resales in its general bank account, where they became commingled with other funds, and, within four months prior to the appointment of a receiver for the corporation, made payments by checks on its general bank account to the finance company for the balances due on such contracts;

> since such payments enabled the finance company to obtain a greater proportion of its indebtedness against the corporation than other general creditors."

Appellee argues that the relinquishment of the right to rescind the sale because of the non-payment of the check was a present consideration for the payment received and in support cites *Illinois Parlor Frame Co. v. Goldman,* 257 Fed., 300 (appellee's br. p. 15). However, appellee overlooks the timing of the transaction in the Illinois *Parlor* case. In that case the relinquishment occurred *on the same day that the alleged preference was received,* which day was *within the four months'* period. The court stated:

> "That appellant did not expressly assert a right of rescision as immaterial; it relinquished that right in confirming the sale; it then gave up a property interest equal to the value of the goods then on hand. To that extent *the transfer was for a present consideration,* and not preferential." (Emphasis supplied.)

In the instant case, however, the relinquishment of any right to rescind, (if any such existed) occurred prior to the commencement of the preferential four months' period when appellee failed to act when the check was not promptly received, failed to act when the check was not paid and acquiesced in the default on these two alleged conditions by redepositing the check which under the doctrine of the above quoted *Frech* case confirmed title in Chemurgy and made Chemurgy *appellee's debtor.* No preferential transfer then took

place—the preferential transfer took place later on February 3rd, 1947 (within the four months' period) and therefore the doctrine of the *Illinois Parlor* case of a transfer for a *present consideration* is not relevant.

On Page 17 appellee attempts to rely upon an allegation of fraud in the transaction, but there is no basis whatsoever in the record for a claim of fraud and the court found none. As stated in the Agreed Statement (Tr. 13) Whitemore's testimony is that it was agreed that a check would be mailed *after* receipt of the warehouse receipt. That the check was not to be mailed until after the warehouse receipt was received is further evidenced by Exhibit A to the Agreed Statement (Tr. 16), being the letter transmitting the warehouse receipt in which Chemurgy was directed to mail a check to Benzel. The mere unexplained failure to immediately transmit a check, which could have been caused by many reasons, certainly raises no inference of fraud and of course the initial non-payment of the check does not indicate that title was obtained by fraud because the title, by agreement of the parties under the warehouse receipt statute (Rem. Rev. Stat. § 3627), vested by delivery of the warehouse receipt *prior to the issuance of the check.* Furthermore, the check when issued was not promptly deposited by Benzel who waited four days before even depositing the check for collection giving plenty of opportunity for the impact of other transactions upon the account of Chemurgy in the Wenatchee bank. This was not a case where an N.S.F. check was used to induce the transfer of possession and title.

Appellee finally contends (appellee's br. p. 21):

> "Benzel had the right upon dishonor of the check to retake the property or *to recover the proceeds* of the sale. *Benzel elected to recover the proceeds* of the sale rather than retake the property. The waiver of the right to Benzel to retake the property is a sufficient present consideration passing to the creditors for the recovery of the proceeds of the sale."

There is absolutely no basis in the record to support the statement that Benzel *elected to, or did,* recover the "proceeds of the sale." The wheat was delivered January 3rd, 1947. Chemurgy was in the business of manufacturing wheat into glucose and there is no evidence whatsoever as to what became of the wheat or that there were any "proceeds" out of the wheat which could have been recovered a month later (February 3, 1947) when Chemurgy's check was paid by its bank.

CONCLUSION

1. The main contention of defendant's brief is that title did not pass to the wheat until the check was paid. This premise is untenable for the following reasons:

a. Title passed when the negotiable warehouse receipt was delivered to Chemurgy (mailed January 3rd, 1947, received January 4th, 1947), Rem. Rev. Stat. § 3627 and § 5836-33, Finding II (Tr. 25), *Goodwin v. Bear,* 122 Wash. 49,209 P. 1080.

b. Even if the sale had been made on condition that a check would be mailed upon delivery of the warehouse receipt, this condition fell and title passed when Benzel

elected not to stand on the condition when it was not satisfied, but accepted a check ten days after delivering the wheat. This election to pass title is further emphasized by the fact that when the check was not paid defendant again did not insist on possession of the wheat but relied upon Chemurgy's promise to pay, thus demonstrating as a matter of law that title passed.

> "Reliance upon a subsequent promise to pay, that leads the seller to refrain from asserting his right to retake the property, is in itself a waiver of the right, and makes absolute a delivery which in the first instance was conditional. The right of plaintiff to recover back his property after he had delivered it resulted from the buyer's failure to keep his first promise. His failure to keep subsequent promises to pay could neither prolong nor revive that right." *Frech v. Lewis,* 218 Pa. 141, 67 Atl. 45.

2. Upon the passing of title on January 3, 1947, an obligation to pay for the wheat arose. Thus, when the check was paid out of the funds of Chemurgy within the four months' period Benzel was a creditor receiving payment upon an obligation arising prior to the four months' period and the Washington preference statute requires that the payment be returned.

> "But absent such a claim (of security), all inquiry regarding the status of a preference is limited to what took place within the four months' period * * * credits received by the insolvent from the creditor prior to the four months' period, unless enjoying statutory priority or secured in some manner, may not be setoff or taken into consideration in any other way, whether or not the insolvent

made a profit on the transaction." *Seattle Association of Credit Men v. Hudson,* 135 Wash. Dec. 643 at p. 647, 214 P.(2d) 681.

The fact that the obligation owing to Benzel arose within the month prior to the four months' period is of course no reason to distinguish this case from the many other cases in which the creditors have been required to return their payments. As a matter of fact, in other cases involved in this bankruptcy the obligations upon which payments were made and which were required to be returned by judgments entered, arose even subsequent to the Benzel obligation. It has been conclusively held that the fact that the creditor does not regard the transaction as an extension of credit is immaterial.

"That the parties did not regard nor intend the transaction as an extension of credit, makes the payment nonetheless a preference." *Seattle Association of Credit Men v. Daniels,* 15 Wn.(2d) 393 at p. 397, 130 P.(2d) 892.

The judgment of the District Court should be reversed with direction to enter judgment for the appellant as prayed for in the complaint.

Respectfully submitted,

Eggerman, Rosling & Williams
DeWitt Williams
Attorneys for Appellant